

Political Economy of Power

- Double problem for study
 - Positive analysis of what has occurred with normative model as an input
 - Systematic and not idiosyncratic account of political economy

Disturbance

Political Economy of Power

- **Baseline**

- Nationalist development (security)
- Electricity as political asset: entitlement and currency (not commodity)
- SOE as opaque bundling of political and economic assets
- Costs of revenue base and cross-subsidies spread unclearly

Political Economy of Power

- **Disturbance (of SOE system)**
 - Marketization and organization reform (corporatization; privatization)
 - Finance
 - *Professional networks*
 - *Technical by-pass (telecom)*
 - *Politically organized interest groups disserved (price or quality)*

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- **Defection**

- Private strategies destabilize
- Segregate political from economic (market) assets
- Self-generation
- Corruption to limit cross-subsidies

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- **Opening** to ideal (normative) model
- **Re-regulation** everywhere
 - Deregulation not yet available in any model
 - Shift in cost of service/ natural monopoly/
integrated utility model incomplete
 - Movement toward marginal cost pricing,
wholesale competition, environment (DSM,
RSP, IRP) grafted into older system

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- **Re-regulation** around a different pattern (than ideal model)
- **Initial Stall**
 - What is the initial disturbance to which the polity is reacting?
 - Not perceived a system problem
 - Partial remedies without commitment to idealized reform beyond its utility to the patch

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- **Path-dependence**

- Organizations adapted to rent seeking strategies
- Political bureaucracy and associated labor with control premia
- Continuing value of political assets as attractor
- Dual business strategies

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- **Complementary** Institutions Absent
 - Capital markets
 - Corporate governance
 - Political governance (corruption)
 - Law
- **Perverse** effects and discrediting
 - FDI behavior on up front cost recovery with expected obsolescence

Political economy of Power

- **Dynamics of partial reforms**
 - Cherry picking
 - Public appropriation of private strategies to separate marketable from political (stranded) assets
- **Preemption** as strategy to cut off defection in anticipation of state as residual holder of stranded assets

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- **Preemption:** formation of wider political coalition to forestall reform completion
- **Stigma:** Foreign reform difficulties and complexities of competitive model
- **Weak Regulatory Capacity**
 - Instruments and Authority
 - Transparency of Object
 - Legal lack of support
 - Capture by residual monopolist

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- **Preemption:** Political (social compact) goals cannot be sustained when unbundled and made transparent
 - External (independent) regulation and transparency of social politics transfers goals from SOE management to legislature
 - Legislature, especially if newly contested, unpredictable
 - Stranded assets best managed opaquely
 - e.g.: Agricultural tariffs moved to state budgets (DSM?)

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- **Political culture (and risk)**
 - Disjuncture between perception of efficiency as lower cost power and reality of higher tariff
 - Capital costs of non-depreciated power
 - Environmental quality
 - Privatization as politically corrupt (FDI) in infrastructure
 - Entitlement loss in commodification

Speculative scenario

SOE dynamics

- SOE's in all 5 countries exhibited in the period from 1960-1985(?) a systematic tendency to build out their infrastructure at (inefficiently?) large scale
- The incentives to do this were in state financing through selective capital access to national bank (soft) loans, international markets with state guarantees, or multinational financial institutions in state sponsored projects

Speculative scenario

SOE dynamics

- This build out has resulted in infrastructure profiles that affect the costs of power across investment cycles
 - There is now substantial aging plant in the national electric systems
 - Much of this plant is fully depreciated and has very low costs
 - Substantial power resources transformed electric power into a political currency for favored groups and interests

Speculative scenario

SOE dynamics

- There is in each country a question of the uses made of the surplus that existed between the price charged (or chargeable) and the low short run marginal costs in the operating system
- The roster of uses described includes:
 - Industrial policy
 - Social policy (e.g. agricultural tariffs)
 - Increasing access (ESKOM)
 - General Treasury revenues (PEMEX/CFE)

Speculative scenario

SOE dynamics

- Roster of uses (continued)
 - Retain in SOE as capital for new infrastructure (China)
 - Sell income stream through privatization of generators (BNDES)
 - Sell through distribution privatizations if wholesale (generation) tariffs are capped
 - In some cases through cross-subsidies or losses absorbed by the SOEs, tariffs were charged below even short run marginal costs (who bore or bears these costs?)

Speculative scenario

SOE dynamics

- The expectations created by the costs associated with the (overbuilt) vintage of infrastructure created by SOEs raises two problems for financing new infrastructure at prospective long run marginal cost
 - Old capital replacement with extraordinary rate of retirement of existing plant
 - Growth to accommodate rising demand

Political Economy of Power

- **Reconsolidate as hybrid system**
 - Market elements (e.g. accountability; generation dis-integration, financial reform) in reorganized political system
 - Dual corporate strategies (political asset value)
 - Political reorganization effects on outcomes
 - Decentralization (central to local authority)
 - Ministries to semi-autonomous (state) corporations or groups

Political Economy of Power

- Single buyer and (renegotiated) contracts
- Muted competition
- Mixed financing (for increasing costs)
- Multiple political equilibria (subsidies, portfolio standards, infrastructure support) with public-private negotiation of terms
- Diffusion by imitation (neighbors) and infra-regional
- Foreign and private investment entry in coalitions (game) with empowered (market/political) hybrids

Political Economy

- **Pathways** beyond hybrid re-regulation
 - Technological disruption of adapted system through altered architecture and organizations (telecom)
 - Accession to international regimes with borrowed institutions
 - Expansion of marginal into core with pervasive marketization
 - International cooperation to support margins